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'Bait-and-Switch' on the Family Credit

Speaker Newt Gingrich recently wrote that the Republican tax-cut bill "categorically rejects the class warfare that has made Democratic tax policy so destructive." In reality, the tax proposals contained in the Contract With America are affirmative action for the rich and bait-and-switch for lower-income working families. These tax cuts will disproportionately favor upper-income taxpayers and will be paid for, if at all, by that silent majority of Americans on whom Gingrich and the Republicans have turned their backs.

The centerpiece of the Republican tax proposal is the $500 per child family tax credit. Gingrich praised the benefits of this supposedly family-friendly proposal as a $500 credit that "treats every child equally and benefits working Americans the most." What he did not say is that this $500 credit will be denied to approximately 10 million working American families with nearly 24 million children.

How did this happen? It happened because Gingrich decided to reduce the maximum amount of the family tax credit available to blue-collar families. The original family tax credit proposal in the Contract With America was more generous to working families—the maximum amount of the credit, regardless of the number of qualifying children, was defined as an amount equal to the sum of the taxpayer's federal income tax liability and Social Security taxes paid in excess of his or her earned income tax credit. In the lexicon of tax lawyers, this is called partial refundability. Introduced in September 1994 and as H.R. 6 in January of 1995, this contract proposal would have helped many working-class families and was in fact more generous than the family tax credits proposed by both President Clinton and Minority Leader Richard Gephardt.

It was not until the third family tax credit proposal, H.R. 1215, introduced on March 13, that a total of 10 million blue-collar families with children had their Contract With America voided by Gingrich's decision to take the money from blue-collar Americans and give it to the rich and powerful. He did this by limiting the maximum amount of the credit to the taxpayer's federal income tax liability. Or, as tax lawyers would say, the credit is nonrefundable.

Almost all of the 10 million families Gingrich has made ineligible for the full $500 family tax credit pay more Social Security tax than federal income tax, but in the speaker's world, the Social Security tax is not really a tax and therefore should not be included when calculating a family's tax burden. Many families who would have received credits under the original contract proposal will receive either much smaller credits or no credit at all under the current Republican bill. Two-thirds of this reduction will come from the 23.3 million families with incomes of less than $50,000.

Why the sudden last-minute change in the legislation? The Republicans claim that the family tax credit was never intended to be even partially refundable and that H.R. 1215 simply corrects drafting errors. If this is true, why did it take three drafts of the legislation, congressional elections and days of hearings on the contract to correct a so-called drafting error? Surely no one thinks that Gingrich did not know that the family tax credit in the first two proposals was partially refundable.

The honest answer is that the Republicans needed the money to provide tax benefits to large corporations and wealthy individuals. By not including partial refundability in the third family tax credit proposal, the Republicans saved $13 billion over five years. Taking $13 billion from working families for deficit reduction might be justifiable, but the Republicans chose to give this money to large corporations in the form of alternative minimum tax (AMT) relief, which the Joint Committee on Taxation has estimated will cost $16.9 billion over five years. The Republicans continue to argue that partial refundability of the family tax credit was never intended to be part of the contract, but by the same measure, neither was alternative minimum tax relief for corporations.

Changes in the AMT for corporations combined with the outrageously expensive corporate depreciation write-off provision in the contract will result in many corporations being able to eliminate most of their federal income tax liability. Some of America's largest and most profitable corporations will be able to skirt most of their tax obligations. It is perverse to take the revenue gained by the removal of a partially refundable family tax credit and redistribute this money to large corporations.

What happens to working families under Gingrich's scheme? Let's look at a family of three, with one child, making $15,000 per year that would have been eligible to receive the $500 family credit under the original proposal in the Contract With America. Under Gingrich's revised bill, this family would receive a family tax credit of $90, a loss of $410 compared with the original contract proposal. A middle-aged divorced mother with three children, earning $20,000 per year, would have received a family credit of $1,500 under the original family tax credit proposal. Under the revised bill, this same mother would receive a family tax credit of only $585, a loss of $915 compared with the original contract proposal.

Under Gingrich's revised bill, it is obvious that every child is not treated equally—and those modest-income families that could truly benefit from a $500-per-child tax credit are not equal partners in the contract.

The movement by more than 100 Republican members of the House to amend the contract and limit the family tax credit to families making $95,000 per year more or less validates Democratic complaints that a family making $200,000 per year is not middle class. But these Republicans still miss the point—lowering the threshold will not put money in the pockets of lower-income working families who will receive nothing from the Contract With America but a broken promise of partial refundability.

Recent polls have shown that the American people do not want Congress to vote for tax cuts before reducing the deficit—especially not ones that bloat the deficit by $630 billion over the next 10 years. However, if tax cuts are politically inevitable, they should be targeted to those working families who are striving to make ends meet. Unfortunately, those families are going to be two-time losers in Gingrich's world. Not only will they receive little or no benefit from the tax cuts contained in the Contract With America. They will also be hardest hit by the Draconian cuts in spending that are necessary to pay for the speaker's "crown jewel."

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